ST 02-0066-GIL 03/28/2002 FOOD, DRUGS & MEDICAL APPLIANCES

Dietary supplements could be classified as food or they could be classified as drugs if the products purport on the label to have medicinal qualities. See86 Ill. Adm. Code 130.310. (This is a GIL).

March 28, 2002

Dear Xxxxx:

This letter is in response to your letter dated December 19, 2001. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), which can be found on the Department's website at www.revenue.state.il.us/Laws/regs/part1200/.

In your letter, you have stated and made inquiry as follows:

COMPANY, a Corporation, with employees, offices and inventory only in the STATES has specific questions as to whether the following transactions would be included when computing gross receipts for collection of sales/Use tax in the State of Illinois.

(1) Receipts from the sale of dietary Supplements designed for human consumption and purchased over-the-counter without prescription.
(2) Reimbursements to the Company from the company's independent distributors for freight charges paid to a third party (common carrier) for goods and merchandise shipped to the distributors when the freight charges are entered as separate item on the sales invoice and the reimbursement does not exceed actual expense paid to a third party (common carrier). All the merchandises are shipped from the Company's warehouses either in STATES.
(3) Receipts from charge for membership that distributors pay for a yearly membership fee. In return for this fee, the distributors (members) are permitted to purchase products from the Company for personal use or for resale.
(4) Receipts from charge for Internet Services where the Company (seller) hosts a server in STATE and creates home page and provides server space for its independent distributors.

Please kindly inform the company of the proper tax treatment of these transactions so that the company may comply with all the requirements of the State regulation. If you have questions, please feel free to call.

The Retailers' Occupation Tax Act imposes a tax upon persons engaged in the business of selling at retail tangible personal property. 35 ILCS 120/2 (2000 State Bar Edition). The Use Tax Act imposes a tax upon the privilege of using in this State tangible personal property purchased at retail from a retailer. 35 ILCS 105/3 (2000 State Bar Edition).

Please find enclosed a copy of 86 Ill. Adm. Code 130.310 regarding the appropriate tax rates for food, drugs, medicines and medical appliances. As you can see at Section 130.310(b)(1), "[a] food is any solid, liquid, powder or item intended by the seller primarily for human internal consumption, whether simple, compound or mixed, including foods such as condiments, spices, seasonings, vitamins, bottled water and ice." A medicine or drug is "any pill, powder, potion, salve, or other preparation intended by the manufacturer for human use and which purports on the label to have medicinal qualities." See Section 130.310(c)(1). Under the above stated definitions, dietary supplements could be classified as food or they could be classified as drugs if the products purport on the label to have medicinal qualities.

Items that meet the appropriate definitions of food, drugs, medicines and medical appliances are taxable at the low State rate of tax, 1% plus applicable local taxes. Products that do not meet the appropriate definitions of food, drugs, medicines and medical appliances, or are food prepared by the vendor for immediate consumption, are taxable at the higher State sales tax rate of 6.25% plus applicable local taxes. Soft drinks are always taxed at the high rate. "Soft drinks" does not include coffee, tea, non-carbonated water, infant formula, milk or milk products, or drinks containing 50% or more natural fruit or vegetable juice.

As a technical proposition, handling charges represent a retailer's cost of doing business, and are consequently always included in gross charges subject to tax. See, 86 Ill. Adm. Code 130.410. However, such charges are often stated in combination with shipping charges. In this case, charges designated as "shipping and handling," as well as delivery or transportation charges in general, are not taxable if it can be shown that they are both separately contracted for and that such charges are actually reflective of the costs of shipping. To the extent that shipping and handling charges exceed the costs of shipping, the charges are subject to tax. As indicated above, charges termed "delivery" or "transportation" charges follow the same principle.

We assume you are selling for resale to your distributors; in that case delivery charges are generally not subject to tax. However, if you are not selling to your distributors for resale, the following information may be helpful. The best evidence that shipping and handling or delivery charges have been contracted for separately by purchasers and retailers are separate contracts for shipping and handling or delivery. However, documentation that demonstrates that purchasers had the option of taking delivery of the property, at the sellers' location for the agreed purchase price, plus an ascertained or ascertainable delivery charge, will suffice. If retailers charge customers shipping and handling or delivery charges that exceed the retailers' cost of providing the transportation or delivery, the excess amount is subject to tax.

Illinois Retailers' Occupation and Use Taxes do not apply to sales, such as membership fees, that do not involve the transfer of tangible personal property to customers. However, if tangible personal property is transferred incident to such sales, this may result in Retailers' Occupation Tax liability and Use Tax liability. See 86 Ill. Adm. Code 130.401.

The Telecommunications Excise Tax is imposed upon the act or privilege of originating or receiving intrastate or interstate telecommunications in Illinois at the rate of 7% of the gross charges for such telecommunications purchased at retail from retailers. See 86 Ill. Adm. Code 495, enclosed.

Pursuant to Section 495.100(a), "gross charge" means the amount paid for the act or privilege of originating or receiving telecommunications in this State and for all services and equipment provided in connection therewith by a retailer, valued in money, whether paid in money or otherwise, including cash credits, services and property of every kind or nature, and shall be determined without any deduction on account of the cost of such telecommunications, the cost of material used, labor or service cost or any other expense whatsoever.

Generally, persons that provide subscribers access to the Internet and who do not, as part of that service, charge customers for the line or other transmission charges which are used to obtain access to the Internet, are not considered to be telecommunications retailers. See 86 Ill. Adm. Code 495.100(d).

It is our general understanding that most Internet access providers do not, as part of their billing, charge customers for such line charges, but instead, pay to their telecommunications providers all transmission costs that they incur in providing the service. Generally, the customers pay to their providers all transmission costs that they incur while using the service. The single monthly fee charged by such retailers, which often represents a flat charge for a package of items including Internet access, E-mail, and electronic newsletters would generally not be subject to the Telecommunications Excise Tax.

However, please note that persons providing customers with the Internet access described above, but who also provide customers the use of 1-800 service, and separately assess customers with per minute charges for the use of such 1-800 numbers, are considered to be telecommunications retailers. Such retailers will incur Telecommunications Excise Tax on charges made for such 1-800 services. If, however, such Internet service providers do not separately assess customers with per minute charges, but pay their own providers for all transmission costs for the 1-800 service, they are not considered to be telecommunications retailers.

If Internet access service providers provide both transmission and data processing services, the charges for each must be disaggregated and separately identified. See 86 Ill. Adm. Code 495.100(c), enclosed. The statute does not require disaggregation on the customers' invoice, however. Therefore, it is the Department's position that so long as the non-telecommunications charges are disaggregated from the telecommunications charges in the retailers' books and records, for audit purposes, such disaggregation need not be shown on the customers' invoice. If the non-telecommunications charges are not disaggregated from the telecommunications charges, the full amount will be subject to Telecommunications Excise Tax. If none of the charges billed were for telecommunications, then none of the charges would be subject to tax.

I hope this information is helpful. The Department of Revenue maintains a website, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b).

Very truly yours,

Melanie A. Jarvis

Associate Counsel

MAJ:msk
Enc.